No. [redacted]

IN THE

Supreme Court of the United States

OCTOBER TERM, 1963

156

CHARLES ORAN MENSIK and
MARY MENSIK,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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To the Honorable, The Chief Justice and Associate Justices of the Supreme Court of the United States:

The petitioners, Charles Oran Mensik and Mary Mensik, pray that a writ of certiorari be issued, to review the decision of the United States Court of Appeals for the Seventh Circuit in the above case.

JUDGMENT AND OPINION OF THE COURTS BELOW.

The judgment and opinion of the Tax Court of the United States appear in the certified record. The opinion of the United States Court of Appeals for the Seventh Circuit issued February 10, 1964. The order denying the petition for rehearing followed on March 17, 1964. The

opinion is not yet reported. The opinion of the Court of Appeals and the order above mentioned appear in the Appendix *infra* (pp. 1a-10a).

JURISDICTION

This petition is timely filed in the Supreme Court of the United States, as it is filed within ninety (90) days of the denial of the petition for rehearing in the United States Court of Appeals for the Seventh Circuit. Jurisdiction of the Court is invoked under 28 U.S.C. 1254 (1).

QUESTIONS PRESENTED

1. Does "favors received or to be received," of no determinable monetary value, or no monetary value at all, satisfy the definition of "income", as defined in the statutes and decisions of this Court?

2. Does the presumption of correctness assigned to the Commissioner's assessment of tax liability obtain conclusiveness, as interpreted in this case, or does it avail only in the absence of countervailing evidence, as interpreted by other circuits?

3. When a basic assessment is sustained only by the presumption of correctness, is not the assessment of a fraud penalty, which has its foundation in the assessment presumed correct, necessarily presumption of fraud?

4. Where a wife signer of a joint return with her spouse is assessed for a fifty per cent fraud penalty of $100,511.17, based on tax assessment in connection with the construction of a business transaction by a corporation, with which she has no connection or knowledge under the evidence, and the assessment is affirmed by the Tax Court and the Court of Appeals on presumption of correctness of the

Commissioner's assessment, and fraud is presumed and not proved by a scintilla of evidence of knowledge or willfulness or corrupt motive, is not the wife being deprived of property and branded with the stigma of fraud as an individual without due process of law and only by unreasonable presumption?

5. When the trial judge expressed incredulity at the testimony of the main witness, does not his refusal to entertain corroborating evidence, on the stated ground that it would be merely cumulative, necessarily assign the same incredulity to evidence he has never considered, in violation of due process?

6. Whether a jeopardy assessment of the original sum of $547,967.55 and an addition to tax for fraud in the amount of $273,983.78 was reduced more than $500,000.00 (over 60% of original assessment of tax and fraud penalties) by stipulation and concession of the respondent Commissioner, and further reduced by decision of the Tax Court to $201,022.33 of tax and $100,511.17 in fraud penalties, and the determination that these lesser amounts due is based upon a claimed presumption of correctness and regularity in the original determination of tax by the Commissioner, and conjecture that money loaned by a corporation to a third party might subsequently inure to the benefit of one of the petitioners, was it not error and denial of due process of law for the Tax Court to arbitrarily reject a petition for rehearing, supported by adequate affidavits showing that the crucial loans were not and could not be income or economic gain to either petitioner?

STATUTES INVOLVED.

Internal Revenue Code of 1954:

Sec. 61. Gross income defined.

(a) *Several Definitions.* — Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

(1) Compensation for services, including fees, commissions, and similar items;

(2) Gross income derived from business;

(3) Gains derived from dealing in property;

• • •

(26 U.S.C., 1958 ed., Sec. 61.)

Sec. 6653. Failure to pay tax

(a) *Negligence or Intentional Disregard of Rules and Regulations With Respect to Income or Gift Taxes.* • • •

(b) *Fraud.*—If any part of the underpayment (as defined in subsection (c)) of the tax required to be shown on a return is due to fraud, there shall be added to the tax an amount equal to 50% of the underpayment. In the case of income taxes and gift taxes, this amount shall be in lieu of any amount determined under subsection (a).

• • •

(26 U.S.C., 1958 ed., Sec. 6653.)

STATEMENT OF THE CASE.

This civil proceeding is a specific items case involving some nine issues and did not involve any theory of net worth in its presentation of proof. This case was initiated in June of 1957 less than 90 days after Petitioners filed their 1956 income tax return at which time taxpay-

ers made all their records available to the Internal Revenue Service. On June 17, 1958 the Respondent Commissioner issued a jeopardy assessment in the total amount of $821,951.33, including additions to tax in the amount of $547,967.55 and fraud penalties of $273,983.78 for the calendar year of 1956. On or about the same day, the Internal Revenue Service served notice of levies on approximately 200 persons predicated upon the aforesaid Jeopardy Assessment thus advising approximately 200 persons including corporations holding property and funds belonging to petitioner that the male taxpayer not only owed Federal Income tax but further the Internal Revenue Service was taking the most drastic course possible to force payment because the tax was in jeopardy. On September 14, 1958 petitioners filed a petition in the Tax Court of the United States for a redetermination of the deficiency, as set forth by the Commissioner of Internal Revenue in his notice of deficiency, and during the course of proceedings prior to trial the Respondent Commissioner conceded errors and inaccuracies in the deficiency assessment of more than 60 per cent of the amounts assessed, amounting to errors of more than $500,000.00 of the asserted tax and penalties. On June 14, 1959, the date of trial, respondent filed a motion for leave to file an amendment to answer, changing [redacted] of the case, as well as the amounts of deficiency, to which petitioners filed objections. The Tax Court overruled petitioners' objections, allowed the amendment to deficiency, and proceeded immediately to trial. The case was heard and the Tax Court entered its decision on January 16, 1962. The Tax Court found a tax deficiency in the amount of $201,022.33 for the taxable year 1956, and an addition to tax for fraud in the amount of $100,511.17. On January 30, 1962 peti-

tioners filed a motion for rehearing (Pet. App. p. 113), which the Tax Court denied on August 22, 1962.

Petitioners filed a petition for review in the United States Court of Appeals for the Seventh Circuit on March 27, 1963. The matter was heard and the Circuit Court entered its decision on February 10, 1964, affirming the decision of the Tax Court of the United States. Petitioners filed a timely petition for rehearing which was denied by the Court of Appeals on March 17, 1964.

When petitioners filed proceedings in the Tax Court of the United States on September 11, 1958, the parties entered into a series of conferences to arrive at stipulations. During the course of these conferences, the Respondent Commissioner agreed to stipulations (Pet. App., pp. 64-65) conceding inaccuracies amounting to well more than half of the amount of the tax assessment, and abandoned more than $300,000.00 of the original assessment of tax in the notice of deficiency. (Pet. App. p. 65).

Preliminary to the taking of evidence in the Tax Court, on the consideration of procedure to be followed, the Respondent was informed that it was the intention of the petitioners to subpoena as a witness formed State Auditor Orville E. Hodge, who was then in prison. After discussion of this and other matters, and upon consideration of the representation by respondent's counsel that the receipt of loans in the sum of $176,312.50 by Hodge would not be contested, the petitioners abandoned their stated proposal to request the issuance of a *writ of habeas corpus ad testificandum*, to secure the presence of Hodge. On the date of trial, the Respondent filed an amended answer which changed its original answer (Pet. App., p. 21), which had asserted the *amount* of specific item #3 as being $176,312.50 and the *source* as "loan transactions" between Or-

ville E. Hodge and the Melvin Building Corporation. The new answer (Pet. App., p. 27) changed the *amount* of this specific item to $206,330.56, and now asserted the *source* to be the "measure" of an alleged payment for a remodeling job by Melvin Building Corporation for City Savings Association, a mutual association, of which the male petitioner was an officer and director. Petitioners filed objection (Pet. App., p. 28) to the amended answer, and the Tax Court denied the objection, allowed respondent to amend the answer, and simultaneously ordered trial to commence. This is a "specific items" case and Petitioners, having marshalled their evidence and witnesses to meet Respondent's original "theory of the case", were taken by surprise when the Tax Court allowed the Respondent to change both the *amount* and *source* of this item.

It was not until after the Court's decision that Petitioners learned that the Tax Court had adopted a theory of the case which the Respondent had led Petitioners to believe would not be in issue, and a petition for rehearing was filed immediately, with annexed affidavits by the attorneys for the Petitioners and by Orville E. Hodge. (See Exs. 4 & 5, Pet. App. pp. 129-130). These affidavits demonstrate that the Petitioners were misled by government counsel into not calling Hodge as a witness.

It is not contested that during the pertinent year, 1956, the male Petitioner was an officer and employee of City Savings Association which offered, as a part of its service to business men and to the general public, the use of its facilities for the cashing of checks in substantial amounts in connection with real estate closings, loans and other transactions, wherein the Association was not a party to the transaction, and no funds of the Association were involved. The record is clear that the male Petitioner rendered such service to the parties involved in this

transaction at issue as item #1, the *lender* being Melvin Building Corporation and the *borrower* being Orville E. Hodge. Petitioner acted in the usual manner as an escrow agent or broker would act for such transactions, and the exhibits documents reflect that the Melvin Building Corporation, upon its delivery of $176,312.50, represented by its execution of 3 checks (Ex. 9, 10, 11, pp. 135-137, Pet. App.), received the corresponding promissory notes executed by Orville E. Hodge, acknowledging his loan from Melvin Building Corporation. (Exs. 6, 7, 8, pp. 132-134 Pet. App.) Exhibit No. 9, a check dated March 12, 1956 in the amount of $76,312.50 was made out to Orville E. Hodge, and this exhibit shows his endorsement and deposit in his bank at Granite City, Illinois two (2) days later, in the regular course of business.

The testimonial evidence further disclosed that Hodge had requested the remaining $100,000.00 in cash. This testimonial evidence was corroborated by documentary evidence, in the form of two (2) $50,000.00 promissory notes made to Melvin Building Corporation and executed by Hodge. Hodge's affidavit, filed in support of the motion for rehearing, acknowledge the receipt of the full $176,312.50, and reaffirmed the aforesaid testimonial and documentary evidence.

The Tax Court in its decision and findings, asserted fraud penalties only in connection with the single item of $176,312.50, and made no such separate findings in connection with the other two items of fraud, asserted by the Commissioner. (Pet. App. pg. 110). It is to be noted that the Court of Appeals, in its decision (A. p. 9a) *infra*, characterized such finding of fraud as being based upon "consideration of the record as a whole", thus misapprehending the decision of the Tax Court, and further misapprehending that petitioners' appeal was based upon the

failure of the record to support the receipt of this single item by petitioners, and the valid contradiction of the presumption of correctness initially attaching the Commissioner's assessment, which the respondent admitted to be in error, both by amended answer and by *stipulation*.

The uncertainty of the Tax Court is evident from the very language of its inconclusive findings. Further these factors and the documentary proof to the contrary notwithstanding, the Tax Court held in regard to the alleged deficiency of $176,312.50 (by amended answer increased to $206,330.56) as follows:

> "Held, further, that petitioner has failed to prove that the income so received was in a lesser amount than determined by respondent in his determination of deficiency. Held, further, that the respondent has failed to carry his burden of proving that the income so received by petitioner was in an amount greater than determined by him in his determination of deficiency." (Pet. App. pg. 30)

And, again:

> "With respect to the first of the issues stated, the respondent has made no concession, but to the contrary, now claims, by amended answer, that the amount in issue should be increased from $176,312.50, as originally determined, to $206,330.50. There is, of course, no presumption of correctness as to the additional amount now claimed, but *as to $176,312.50* covered in respondent's determination of deficiency, *the presumption of correctness continues.*" (App. 66) (Emphasis supplied.)

And, further:

> "Also, we are persuaded and convinced that they were made with the deliberate purpose of providing funds for the payments made to him by Melvin, whether they were intended for him *or* for Hodge, or whether they

came to rest with him or were passed on to Hodge. What the arrangement *was* between petitioner and Hodge, *we do not know*. It *could be* that a pay-off to Hodge for favors received or to be received by petitioner or his wholly-owned loan companies was made. *Whatever they were*, and to the extent they did occur, we are satisfied that they were advisedly arranged for and made by petitioner, and *there is no evidence of record* which persuades us that there was any intention that such payments which did reach Hodge, *if any*, were to be repaid." (App. 94) (Emphasis supplied.)

Aside from the foregoing documentary proof that trial Judge did not regard as reliable the male petitioner's testimony and even though the Respondent introduced no evidence or documents to contradict taxpayer's position the Tax Court held that the "presumption of correctness" supported the assessment. This situation obtained as to the other items in issue notwithstanding the proof both testimonial and documentary, introduced by Petitioners as to each and every issue. Thus, the Tax Court found that, on the presumption of correctness, the petitioners were to be assessed $176,312.50. Though the Commissioner alleged fraud in three items, one for the $176,312.50, another of $10,000.00, and a third in the amount of $6,800.00 (Pet. App. pg. 110), the Tax Court found fraud only in the item of $176,312.50 (Pet. App. pg. 111-113). The Court of Appeals for the Seventh Circuit held that the "record as a whole" supported the finding of fraud by the Tax Court. (Ap. p. 7a) *infra*. This was contrary to the finding of the Tax Court, which made the specific item of $176,312.50 the sole basis for its finding of fraud.

REASONS FOR GRANTING THE WRIT.

I.

The decision of the Tax Court, endorsed by the affirmance of the Court of Appeals, that "favors received or to be received" of no determinable monetary value, or no monetary value at all, satisfies the definition of "income", is contrary to the statute and in conflict with applicable decisions of this Court.

The Tax Court found:

> "• • • What the arrangement was between petitioner and Hodge, *we do not know*. It could be that a pay-off to Hodge, *for favors* received or *to be received* by petitioner or his wholly-owned loan companies was made. Whatever they were, and to the extent they did occur, we are satisfied that they were advisedly arranged for and made by petitioner, • • • (Pet. App. pg. 94) (Emphasis supplied.)

To sustain a finding of the receipt of taxable income it is not enough for a Tax Court to say it does in its opinion that this $176,312.50, which Hodge received, could be for "Prior Favors" received or "to be" received from Hodge by the Petitioners or the loan associations in which they held shares. There is here no measurable economic gain that can be ascertained by the receipt of "favors" and the Tax Court erred in its finding that such amount constituted the receipt of "taxable income" to petitioners. We respectfully submit that to assess petitioners with the obligation to pay additions to tax on the basis of such a finding would deprive petitioners of property in violation of their constitutional rights of Due Process of Law.

Analyzing this uncertain decision of the Tax Court, the most concrete thing said is that the Tax Court considered that this might have been a "pay-off" to Hodge for favors received or to be received. It is our submission that such an interpretation of "income", under the Sixteenth Amendment and under 26 U. S. C., Sec. 61, is contrary to law and a perversion of both the Constitution and the Statute. The Sixteenth Amendment is a grant of power for the taxation of income. Under it, that may not be taxed which is not "income". *Eisner* v. *Macomber*, 252 U. S. 189; *M. E. Blatt Co.* v. *United States*, 305 U. S. 267. This Court also found in *Helvering* v. *Stuart*, 317 U. S. 154, that:

> "Economic gain realizable by the taxpayer is necessary to produce a taxable income under our statutory scheme."

Further, in *Merchants L. & T. Co.* v. *Smietanka*, 255 U. S. 509, this Court said at p. 519:

> "In determining the definition of the word 'income' thus arrived at, this Court has consistently refused to enter into the refinement of lexicographers or economists, and as a proof, in the definitions quoted, what it believes to be the commonly understood meaning of the term which must have been in the minds of the people when they adopted the Sixteenth Amendment to the Constitution."

The Tax Court by its own language, see (Pet. App. pg. 94) • • • "We do not know what the full and true story is with respect to the payments by Melvin to petitioner in 1956." • • • "What the arrangement was between petitioner and Hodge we do not know." • • • "Whatever they were, and to the extent that they did occur • • •" (Pet. App. pg. 95) • • • "Frankly, considering the state of the record, we do not know what the truth is" • • •.

clearly demonstrates its own confusion, conjecture and uncertainty. The decision of the trial court, affirmed by the Court of Appeals, has here resulted in a crushing assessment of tax and penalties against these petitioners placing them in financial jeopardy to pay more than $300,000.00 in a proceeding that has so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision.

On the basis of the statutes, and on the cases decided by this Court, including those adverted to hereinbefore, we respectfully submit that the decision of the Tax Court in this case, as approved by the Court of Appeals for the Seventh Circuit, constitutes a decision on a federal question in a way in direct conflict with the applicable decisions of this Court, and, on that account, certiorari should be granted.

II.

In this case, the presumption of correctness assigned to the Commissioner's assessment of tax liability was the only factor that supported the decision, even though there was contravening evidence adduced as to each item comprising the assessment. This decision is in conflict with decisions of other Court of Appeal on the same matter.

The assessment filed herein is comprised of eight items in issue. As to the three most substantial of them, the Tax Court found as follows:

> (1) "Held, further, that petitioner has failed to prove that the income so received was in a lesser amount than determined by Respondent in his determination of deficiency. Held, further, that the Respondent has failed to carry his burden of proving that the income so received by Petitioner was in an amount greater than determined by him in his determination of deficiency." (Pet. App. pg 39)

(2) "The Respondent determined that by reason of the receipt of the $10,000.00 in 1956, petitioner realized income in that amount. Held, that petitioner has failed to show by convincing or persuasive proof that the Respondent erred in his determination." (Pet. App. pg. 31)

(3) "Held, that petitioner has failed to prove that the Respondent erred." (Pet. App. pg. 32)

As to each of these items, and as to all the others, the petitioners introduced proof, both testimonial and documentary. Notwithstanding the proof introduced, this Court will see, as demonstrated herein, that the original assessment found its support in the Tax Court merely on the presumption of correctness which attached to the notice of deficiency made by the Commissioner.

This record is devoid of any showing that the petitioners received taxable income, *even by constructive receipt*, in connection with the checks issued by the Melvin Building Corporation in the amount of $176,312.50, which Orville E. Hodge received, and acknowledged by his execution of corresponding promissory notes, introduced in the trial of this case below Ex. Nos. 6, 7, & 8, (Pet. App. pp. 132-134)[1] There was no showing by Respondent that revenue agents were able to demonstrate through their analysis of petitioners' bank accounts and flow of funds that *any part* of this amount was received by the taxpayer or his wife. The record is clear that petitioners did not receive this money.

[1] The Commissioner of Internal Revenue has assessed Orville E. Hodge for the full amount to the penny ($176,312.50 as taxable income to him for this same year, and has disallowed the lender of the money, Melvin Building Corporation, a "bad debt" deduction for the identical amount loaned to Hodge for this same year. There is no mistaking this item because the amount is precisely identical in the case of each assessment and corrected assessment.

It is fundamental that the Tax Court must give proper credit to unimpeached uncontradicted evidence and may not arbitrarily disregard such testimony or documents in violation of recognized judicial standards and procedures and due processes inherent in our laws.

It is our respectful submission that such a determination is in conflict with other circuits, including the following:

> "While there is a presumption that the action of the Commissioner is correct, that presumption disappears when evidence is introduced to overcome it." *Kentucky Trust Co.* v. *Glenn*, 6 Cir., 217 F. 2d 452-465.

See also *Collings' Estate* v. *United States*, W. D. Ky., 138 F. Supp. 837-841; *Manchester Board & Paper Co.* v. *C.I.R.*, 4 Cir., 89 F. 2d 313; *Woodward* v. *United States*, 106 F. Supp. 14, aff'd., 8 Cir., 208 F. 2d 893.

III.

In this cause, the basic assessment was sustained only by a presumption of correctness attached to the notice of deficiency, notwithstanding the admitted error in excess of $500,000.00 (over 60% of original assessment of tax and fraud penalties). The Court relied only on the presumption of correctness. On that basic assessment, presumed correct, a fraud penalty was further assessed. It is our submission that this constitutes presumption of fraud, contrary to applicable decisions of this Court, and in conflict with the decisions of other Courts of Appeal on the same subject.

We submit to the Court that the burden of proof, being an understatement of income motivated by fraud, was, in accordance with general decisions, incumbent upon the Commissioner-Respondent. But, before it can be said that

an understatement was fraudulent, the understatement itself must be proved, and not presumed. Presuming one of the vital elements of the burden that was the Commissioner's necessarily constitutes a *presumption* of fraud.

The fraud penalty was added by the Tax Court to the assessment of tax against the petitioners by reason of failure to report a sum that the Hodge affidavit (Pet. App. pg. 127), and the Commissioner's Notice of Deficiency to Hodge show have been assessed as taxable income against him. Undeniably the record shows that Melvin Building Corporation paid tax on the $176,312.50 when its claim of deduction in its 1956 income tax return (see Trial Exhibit S) for Hodge's bad debt was disallowed. There is no mistaking the fund for the figure is the same in the case of each assessment, and corrected assessment.

This demonstrates beyond argument that the disclosure by Melvin of the amounts in its 1956 income tax return claiming deduction for Hodge's bad debt, the delivery of notes by Hodge to Melvin for the amount, the book entries by Melvin concerning the loans and the ready testimony of all parties concerned, dispel any claim of concealment. There was rather an abundant disclosure which led to three assessments of tax on the same item in three investigations of the parties. Even if all of these assessments are to be treated initially as presumably correct, unreasonable presumption fails, when contradicted validly, or when it departs from reason and experience. (See *Tot* v. *United States*, 319 U.S. 463, 467-469; 87 L. Ed. 1519, 1524, 1525.)

We respectfully submit that the decision of the Tax Court, affirmed by the Court of Appeals for the Seventh Circuit, is contrary to this Court's decision in *Vitelli & Son* v. *United States*, 250 U.S. 355, which case is a land-

mark decision that fraud must be found, without reference to any presumption of law or fact.

We further submit that the decision of the Tax Court and of the Court of Appeals in this cause is contrary to the holding of the Sixth Circuit in *Hawkins* v. *C.I.R.*, 234 F. 2d 359, 360, and to the holding of the Third Circuit in *Valetti* v. *C.I.R.*, 260 F. 2d 185, 188.

This Court's particular attention is directed to a comparison between this case and *Goldberg* v. *C.I.R.*, 5 Cir., 239 F. 2d 316.

In the *Goldberg* case, the Fifth Circuit restated some of the Tax Court's findings, which reflect a definite similarity with the findings here:

> "As to the legal expense, the Tax Court disallowed the deduction and said. 'For aught the record shows, some, if not all, of the legal expenses involved might very well have been and probably were, incurred in defending criminal actions against petitioner or his employees, or securing their release from custody, or in regaining possession of slot machines which had been confiscated.' These inferences were made by the Tax Court in sustaining the tax deficiencies where the petitioner had the burden of proof and the Commissioner had the benefit of a presumption. They can hardly be regarded as showing or tending to show a specific fraudulent intent to evade income taxes."
>
> *Goldberg* v. *C.I.R.*, 239 F. 2d 316, 321.

In the instant case, the Tax Court found:

> "• • • they were made with the deliberate purpose of providing funds for the payments made to him by Melvin, whether they were intended for him or for Hodge, or whether they came to rest with him or were passed on to Hodge. What the arrangement was between petitioner and Hodge, we do not know. It could

be that a pay-off to Hodge for favors received or to be received by petitioner or his wholly-owned loan companies was made. Whatever they were, and to the extent they did occur, • • •" (Pet. App. pg. 94).

The Tax Court further found (Pet. App. pg. 112):

• • • "Accordingly we are satisfied and convinced that *if any* of the funds so received by petitioner from Melvin were in turn paid over to Hodge with any understanding between him and Hodge that repayment was to be made, it was petitioner's purpose and intent that in whole or substantial part he *would be* the ultimate recipient. And insofar as the funds purportedly loaned to petitioner represented funds diverted from City Savings under the guise of payments for the remodeling of its building the same is true as with respect to the purported loans to Hodge • • •". (Emphasis supplied.)

It is respectfully submitted that this language of the Tax Court in its decision which was affirmed by the Court of Appeals "in all respects," clearly demonstrates that Petitioners are being assessed additions to tax and fraud penalties in violation of Due Process of Law by a Court which finds;

1. That it is not certain of the amount involved on construction work by a corporation;
2. That it is not certain who received the money;
3. That holds; Even if the Petitioners did not receive the money, one of them must have intended to become its ultimate recipient.

IV

The assessment of a fraud penalty against the wife signer, who under this record had no connection with, or knowledge of, any of the transactions with which the evidence was concerned, is in conflict with the decision of other Courts of Appeals on the same matter.

In this cause, Mrs. Mary Mensik filed a joint return with her husband, Charles Oran Mensik. She was assessed with a 50% fraud penalty of $100,511.17, based on a tax assessment in connection with the construction of a business transaction by a corporation with which she had no connection or knowledge under the evidence. This assessment against Mrs. Mensik was affirmed by the Tax Court and the Court of Appeals for the Seventh Circuit on a presumption of correctness of the Commissioner's assessment, as has been discussed hereinbefore. Not one scintilla of evidence of knowledge of these transactions, much less willfulness or corrupt motive, finds support in the evidence as to Mrs. Mensik. It is our submission that she has been deprived of property, and branded with the stigma of fraud as an individual, without Due Process of Law and only by an unreasonable presumption.

There is no mention of the conduct of Mrs. Mensik in the record which is completely bare of evidence of any kind or nature offered by the Respondent in connection with the burden of proof, which is a requirement to be satisfied by the Respondent to sustain the imposition of fraud penalties against this petitioner.

The Revenue Acts as passed by the Congress apply to individuals throughout the nation and further the separate State Laws vary in the matter of property rights of a spouse. It is respectfully submitted that this issue presents a matter of vital importance in the public interest and when a wife signs a joint return where fraud penalties

are subsequently asserted because of the conduct of a husband in connection with his receipt of income even if it be unknown to her, an unfair obligation of payment places such person in complete financial jeopardy. Further, upon divorce or in the event of the death of her spouse she, without fault, is faced with crushing penalties and obligations to pay amounts impossible for her to meet. Should such divorced person or widow remarry her new spouse could become subject to tremendous financial obligations not contemplated by him at the time of such marriage. We respectfully submit this constitutes an important question in Federal Law, which has not been, but should be, settled by this Court.

There is absolutely no evidence or presumption to support imposition of fraud penalty against Mary Mensik. The Commissioner-Respondent did not prove or *state* one iota or scintilla of fact that would indicate his intention to contend her conduct was fraudulent. (See *Cirillo* v. *C.I.R.*, 314 F. 2d 478, 484.)

The original assessment having been upheld by a presumption of correctness, and the female petitioner's [Mrs. Mary Mensik's] liability being created by a similar presumption, offends against basic legal concepts of the requirements for assertions of fraud penalties and established standards of proof in derogation of Petitioner's constitutional rights of Due Process of Law.

V.

The main witness in this cause was the male petitioner. The trial Judge expressed incredulity at his testimony, and then refused to entertain corroborating evidence, on the stated ground that it would be merely cumulative.

Hodge's testimony and affidavit (Pet. App. pp. 121-122, 127-128) shows unequivocally that he received loans from Melvin in the amounts in debate, and described the manner in which each amount, comprising the total sum of $176,312.50 was received by him.[2]

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[2] See transcript of testimony of Orville E. Hodge, taken at Illinois State Penitentiary, Menard Branch, Menard, Illinois, by agents of the Internal Revenue Service, at a time when neither the petitioners nor their attorneys were present (Pet. App. pp. 121-122):

"Q. How were you able to acquire so much money from and through Mr. Mensik, Mr. Hodge, during the periods we have discussed?

"A. My only answer is that I had the collateral to back up a loan.

"Q. Could these so-called loans have represented a consideration for any favor that you have granted Mr. Mensik or his association?

"A. I never gave Mr. Mensik any more favors than I gave any other loan Associations in Chicago or the State of Illinois.

"Q. He did, however, get two charters for stock—

"A. He didn't get these from me directly. He got them from the committee.

"Q. You approved them?

"A. I didn't- the committee did.

"Q. As State Auditor, didn't you have to approve them?

"A. I didn't approve them. I signed them after their approval."

Also, see Affidavit of Orville E. Hodge, annexed to Petitioner's petition for rehearing in the Tax Court. (Pet. App. pp. 127-128)

"That, in the course of building the Esquire Hotel in Florida, affiant borrowed $176,312.50 from Melvin Building Corporation. This amount was used by your affiant for such purpose. This money was received from the Melvin Building Corporation and, for this amount, your affiant signed certain promissory notes. Affiant further states that he intended to pay this money back to Melvin Building Corporation within a year. Affiant had also borrowed $200,000.00 from City Savings Association in Chicago, Illinois, and affi-

The Tax Court Judge, concurred in by the Seventh Circuit Court of Appeals, viewed this aspect of the case as follows: (See comment of Tax Court Judge on denial of rehearing (P. 36, Tr. Aug. 22, 1962).

> "The Court dealt with the issue in that posture and the Court said very plainly that on the record in this case and on the evidence, the *answer* would be the same, whether or not Hodge received the money as a *bona fide loan or* whether he *didn't* receive it. And the Court is still of the view that the record is ample and adequate to support and sustain the findings he made in the decision, and that if Hodge were called as petitioner now desires, to testify that he did receive the money as a loan; that would not change the disposition of the case, and I think that the Opinion amply shows that.
>
> "The situation being as it is, the motion for rehearing is denied."
>
> "All right, the ruling has been made on the motion, and we will stand adjourned." (Emphasis supplied)

(Continued)

ant had given as security for this money a first mortgage on the Esquire Hotel. Your affiant states that, if he were unable to pay back the $176,312.50 to Melvin Building Corporation within the year, affiant intended to issue a second mortgage to Melvin Building Corporation on the Esquire Hotel in Miami, Florida. Affiant states that the said Hotel, in affiant's opinion, was worth at least $700,000.00, and that, at a forced sale, and under peculiar circumstances, it was sold for $575,000.00. Affiant felt that a total mortgage of the amount of $376,312.50 was an amount well within the actual value of said property.

"Your affiant regarded the loan from Melvin Building Corporation as a pure business deal, and your affiant, in his private and official capacities, did no favors for C. Oran Mensik in return for the loan of this money or any other monies."

It does violence to reason for the Tax Court to say as it did: "The answer would be the same whether or not Hodge received the money as a bona fide loan or whether he didn't receive it." (Emphasis supplied) Logic dictates that the answer could not be the same because the bona-fide Loan from Melvin Building Corporation to Hodge could not be receipt of taxable income by petitioners. Due Process is an absolute constitutional guarantee and the refusal of the trial court to allow Petitioners to call this vital witness Hodge, to acknowledge that he received the money, was an abuse of its discretion and a clear violation of Petitioner's right of Due Process of Law.

We respectfully submit that it is a necessary deduction from the action of the trial court that he assigned incredulity to evidence he refused to consider, in violation of Due Process of Law and in violation of his clear obligation to weigh the evidence.

VI.

Preliminary to the taking of evidence in this case, on the consideration of procedure to be followed, the Court was informed that it was the intention of the petitioners to subpoena as a witness a former State Auditor Hodge, who was then in prison. After discussion of this and other matters with government counsel, and upon the representation by government counsel that the receipt of loans in the sum of $176,312.50 by Hodge would not be contested, the petitioners abandoned their thought of requesting subpoena for Hodge.

It was not until after the Court's decision that petitioners learned that the Tax Court had adopted a theory of the case which the Respondent had led petitioners to believe would not be in issue, and a petition for rehear-

ing was filed immediately, with annexed affidavits by the attorneys for the petitioners and by Orville E. Hodge. (See Exhibits 4 and 5, Pet. App. pp. 129-130). These affidavits definitely demonstrate that the petitioners were misled by government counsel into not calling Hodge as a witness.

Hodge's affidavit (Pet. App. pg. 127), as annexed to Petitioners' petition for rehearing, shows unequivocally that he received loans from Melvin in the exact amount in issue, and described the manner in which each amount comprising the total sum of $176,312.50 was received by him. In the view taken by the Tax Court Judge of this aspect of the case Hodge's testimony, in accordance with his affidavit, would have been *crucial testimony*. Hodge would have been available for cross-examination. The opportunity for the Judge to consider his manner of testimony, his memory, and his general demeanor, factors considered so important in the decision of the lower court, was a vital factor, to which the Tax Court Judge refused to expose himself. The Tax Court's failure to grant rehearing after decision, in the face of compelling proof by affidavits that justice required such motion be granted, was not a mere exercise of discretion, but an unfounded abuse of discretion.

Further corroboration by documentary evidence was introduced in the form of two (2) promissory notes executed by Hodge to Melvin, each in the amount of $50,000.00 in receipt of $100,000.00 by Hodge (Pet. App. pp. 133, 134, Ex. 7 and 8). This amount together with the check to Hodge from Melvin for $76,312.50 made a total of $176,312.50, the full amount of this item.

The complete disregard of evidence by the Tax Court includes a total failure to explain any conclusion it reached, if any, concerning the check of Melvin for $76,312.50 payable to Hodge and endorsed by him and deposited in his own bank at Granite City, Illinois, and which was one of the loans comprising the total of $176,312.50 loaned by Melvin to Hodge (Pet. App. pg. 135, Exhibit #9). Apparently since the Tax Court could not rationalize this item into its findings and conclusions, it ignored it.

We submit that such a determination and preclusion of evidence on behalf of these Petitioners so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision.

CONCLUSION.

The decision of the Court below has decided federal questions in conflict with decisions of other United States Circuit Courts of Appeal and in conflict with applicable decisions of this Court and has so far departed from the accepted and usual course of judicial proceedings and sanctioned such departures by the Tax Court of the United States in its trial of this case as to call for an exercise of this Court's power of supervision. For the reasons stated, it is respectfully submitted that this petition for writ of certiorari should be granted.

Respectfully submitted,

KENNETH T. JAMES,
Attorney for Petitioners.

APPENDIX A

IN THE

UNITED STATES COURT OF APPEALS

FOR THE SEVENTH CIRCUIT

No. 14167 SEPTEMBER TERM, 1963—JANUARY SESSION, 1964

CHARLES ORAN MENSIK and MARY MENSIK,
Petitioners,
v.
COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Petition to Review the Decision of the Tax Court of the United States.

February 10, 1964

Before HASTINGS, *Chief Judge*, SCHNACKENBERG and SWYGERT, *Circuit Judges*.

HASTINGS, *Chief Judge*. This case is before us on petition of Charles Oran Mensik and Mary Mensik, his wife, for review of a decision of the Tax Court of the United States. *Mensik v. Commissioner of Internal Revenue*, 37 T. C. 703 (1962).

The Commissioner of Internal Revenue, respondent, assessed petitioners a tax deficiency of $547,907.55 for the taxable year ending December 31, 1956, and a fifty per cent

penalty for fraud of $273,983.78, as provided in Section 6653(b) of the Internal Revenue Code of 1954, 26 U.S.C.A. §1221 (1958 ed.).[1]

The decision of the Tax Court ordered petitioners to pay $201,022.33 income tax deficiency and $100,511.17 fraud penalty.

The Tax Court's preface to its opinion concisely states the case by setting out the following general findings of fact and holdings:

> "1. Petitioner [Charles Oran Mensik] as managing officer, president, and chairman of the board of directors of the City Savings Association, employed Melvin Building Corporation to do remodeling of the building of City Savings and in payment therefor caused City Savings to make a gross overpayment for the work actually done, which overpayment was advisedly arranged by petitioner. At or near various dates on which the final payments were being made by City Savings to Melvin, petitioner arranged with Melvin to deliver to him various substantial sums of money as purported loans to him and one Orville Hodge, then State auditor for the State of Illinois. The respondent in his determination of deficiency determined that to the extent of $176,312.50 the moneys so paid over to petitioner constituted income to him. By amended answer, it is his claim that this amount should be increased to $206,330.56. *Held*, that some part, if not all, of the overpayment made by City Savings to Melvin was thereafter paid over by Melvin to petitioner and was income to him. *Held, further*, that petitioner has failed to prove that the income so received was in a

---

[1] "§6653. Failure to pay tax

* * *

"(b) Fraud.—If any part of any underpayment * * * of tax required to be shown on a return is due to fraud, there shall be added to the tax an amount equal to 50 per cent of the underpayment. * * *"

lesser amount than determined by respondent in his determination of deficiency. *Held, further*, that the respondent has failed to carry his burden of proving that the income so received by petitioner was in an amount greater than determined by him in his determination of deficiency.

"2. In October of 1954, Melvin Building Corporation entered into a contract with petitioner's sister for the purchase of 13 lots on West Jackson Boulevard in Chicago, and made a substantial cash payment on the purchase price. The entries on its books reflected only the purchase of lots 2 to 13, inclusive. Early in 1956, Melvin began construction of a building on some or all of the lots including lot 1, and received a construction loan from City Savings therefor. On May 25, 1956, after substantial amounts had been advanced on the loan and the construction was under way, Melvin issued a check for $10,000 to petitioner and entered the payment on its books as payment for lot 1. On March 11, 1957, petitioner, by check, made a payment of $10,000 to Melvin, which check Melvin credited to its notes receivable account. It is petitioner's testimony and claim that the $10,000 paid in March of 1957 was a repayment of the $10,000 received in May of 1956, the repayment being made after discovery that Melvin already owned lot 1. No change in the application of the payment of $10,000 in May of 1956 or in receipt of $10,000 in March of 1957 has ever been made on Melvin's books. The respondent determined that by reason of the receipt of the $10,000 in 1956, petitioner realized income in that amount. *Held*, that petitioner has failed to show by convincing or persuasive proof that the respondent erred in his determination.

"3. In 1956, petitioner caused a check to be drawn on a bank account of City Savings Association for $6,800. The payee shown was Commercial Broadcasters and the basis for the drawing of the check was an invoice made out on a form of Commercial Broad-

casters. The invoice was not the invoice of Commercial Broadcasters and Commercial Broadcasters never received the check. Commercial Broadcasters did not arrange a program or programs such as were described on the bogus invoice. The respondent determined that by reason of the $6,800 payment by City Savings, petitioner realized income in that amount. *Held*, that petitioner has failed to prove that the respondent erred.

"4. Through his relations with City Savings and with Melvin and other institutions with which he occupied dominant positions, petitioner regularly carried on varied business operations, which included the purchase and sale of real estate. *Held*, that the parcels of real estate sold by petitioner in 1956 were sold to customers in the ordinary course of his business, and that the gain therefrom was not capital gain, but ordinary income. *Held, further*, that the income derived from the purchase of real estate tax certificates and their subsequent redemption was ordinary income.

"5. During 1956 petitioner, in the course of his business, sold insurance policies to his employees, to employees of City Savings, and to relatives and friends, on which sales he waived his commissions in favor of the purchasers. The respondent determined that petitioner realized income in the amount of the commissions waived. *Held*, that respondent did not err in his determination.

"6. In June of 1955, petitioner organized the First Guarantee Savings Association, of which he owned 98.8 percent of its stock, and the Chicago Guarantee Savings Association, of which he owned 98.6 percent of the stock. On July 1, 1955, he executed written instruments with each of the associations, reciting that he agreed to spend $55,000 in advertising each such association during the period July 1, 1955, and June 30, 1956. In each instrument it was recited that the association would recommend and give all of the insurance of its members and its own to petitioner for a

period of 5 years, and for an additional 5 years, if $100,000 in commissions was not received by petitioner during the first 5 years. Petitioner expended $17,295.14 in 1955 and $32,076.14 in 1956 for advertising of First Guarantee, and $18,374.84 in 1955 and $36,284.84 in 1956 for advertising Chicago Guarantee. In 1956 he deducted as advertising expenses of his operations carried on under the name of City Insurance Agency, $8,951.93, which was the same in amount as the sum of $5,139.81 received in 1956 in the form of commissions on insurance business originating with First Guarantee and $3,812.12 on business originating with Chicago Guarantee. *Held*, that the amounts expended by petitioner in 1955 and 1956 in advertising the two savings associations represented capital contributions by him to the associations.

"7. In June of 1955, when Chicago Guarantee Savings Association was organized, petitioner paid $9,000 as rent for 20 months for space to be occupied by the association, for $2,000 of which he was reimbursed. In reporting his income for 1955, petitioner deducted as rent $2,700 of the $7,000 net balance, and in his 1956 return deducted the remaining $4,300. *Held*, that the $7,000 so expended by petitioner in June of 1955 was a capital contribution by him to Chicago Guarantee.

"8. In September of 1956, petitioner received premium refunds of $6,166.42 from the insurer of the buildings of First Guarantee Savings Association and Chicago Guarantee Savings Association, this insurance having been sold by petitioner to the associations in the course of his personal business operations. The amounts so received by petitioner were retained by him and have never been paid over to the said associations. *Held*, that the respondent did not err in determining that petitioner realized income in 1956 in the amount of insurance premiums so refunded and received by him." 37 T. C. at 703-705.

The Tax Court then follows with nineteen pages of particularized findings of fact in support of the above general findings. *Id.* at 706-724. These findings are incorporated in this opinion by reference thereto.

Reference is further made to the Tax Court's extended opinion by Judge Turner. *Id.* at 724-754.

On appeal, these findings of the Tax Court must stand unless shown to be clearly erroneous. *Commissioner* v. *Duberstein*, 363 U.S. 278, 291 (1960); *Interstate Drop Forge Company* v. *Commissioner of Internal Revenue*, 7 Cir., ... F. 2d ..... (January 7, 1964).

Petitioners contend "that the Tax Court's findings of fact and law constitute erroneous legal conclusions reversible as a matter of law." After consideration of the briefs, oral argument of counsel, the opinion of the Tax Court and the record as a whole, we hold that there was substantial evidence to support the Tax Court's findings and that the Tax Court did not err in holding petitioners liable for income tax deficiencies in the amount of $201,022.33. *Zeddies* v. *C.I.R.*, 7 Cir., 264 F. 2d 129, 126 (1959), cert. denied, 360 U.S. 910, rehearing denied, 361 U.S. 855.

Petitioners also contend that the Tax Court erred in finding that "a part of the deficiency is due to fraud" and assessing a fifty per cent penalty. Under Section 6653(b) of the Code, *supra* n.1, the fifty per cent penalty may be assessed against the entire deficiency, even though the finding of fraud relates only to part of the deficiency. The burden of proving fraud is on the Commissioner. *Paddock* v. *United States*, 2 Cir., 280 F. 2d 563, 565 (1960).

Civil fraud need not be proved beyond a reasonable doubt, but it must be established by clear and convincing evidence. *Spies* v. *United States*, 317 U.S. 492, 495 (1943);

Zeddies v. *C.I.R.*, 7 Cir., 264 F. 2d at 127; *Karnick* v. *Commissioner of Internal Revenue*, 6 Cir., 232 F. 2d 678, 681 (1956).

The question of fraud is one of fact and the Tax Court's finding is entitled to finality unless it is clearly erroneous. *Bodoglau* v. *Commissioner of Internal Revenue*, 7 Cir., 230 F. 2d 336, 341 (1956); Int. Rev. Code of 1954, §7482. We find convincing evidence in the record as a whole to support the finding of fraud. We hold that the Tax Court did not err in assessing a fifty per cent penalty on the entire tax deficiency. 37 T. C. at 752-754.

Petitioners further contend that the Tax Court twice abused its discretion in the trial of the case.

The Tax Court, over objection of petitioners, granted the Commissioner's motion for leave to file an amendment to his answer to petitioners' petition. The amendment alleged facts concerning an additional item which supported the Commissioner's determination of fraud. Petitioners contend that they were not given sufficient time to meet this allegation.

"The [Tax] Court may at any time, during the course of the trial on the merits grant a motion of either party to amend its pleadings to conform to the proof . . . ." Tax Court Rule 17(d). *C.I.R.* v. *Finley*, 10 Cir., 265 F. 2d 885, 888 (1959), held that this rule allowed amendment at any time before a final decision, and held that an amendment was proper even though made several months after the taking of testimony. In the present case, the amendment was filed *prior to trial*. We hold that the Tax Court's allowance of the Commission's motion to amend was a proper exercise of discretion and petitioners had sufficient opportunity to defend this additional allegation of fraud.

The second abuse of discretion asserted by petitioners was the Tax Court's denial of petitioners' motion for rehearing. An exercise of discretion by the Tax Court in denying a motion to reopen a case will not be reversed on appeal unless there is a showing of extraordinary circumstances. *ABC Realty Company* v. *C.I.R.*, 8 Cir., 295 F. 2d 98, 107 (1961). We have carefully examined petitioners' motion and the three accompanying affidavits. It is our conclusion that no circumstances are demonstrated which show an abuse of discretion by the Tax Court.

We have deemed it unnecessary to engage in a detailed statement of the evidence in this case, in view of our reference to the decision of the Tax Court. It is sufficient for us to say that based on our consideration of the record as a whole, with deference to the trier of fact in the determination of matters of credibility and weight to be assigned to various items of evidence, we are convinced that the deficiencies assessed and the finding of fraud have ample support in the record and must be affirmed. We find no prejudicial error therein.

The decision of the Tax Court is in all respects affirmed.

AFFIRMED.

APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT
Chicago 10, Illinois

Monday, February 10, 1964
Before
Hon. JOHN S. HASTINGS, *Chief Judge*
Hon. ELMER J. SCHNACKENBERG, *Circuit Judge*
Hon. LUTHER M. SWYGERT, *Circuit Judge*

Charles Oran Mensik and Mary Mensik, *Petitioners*, vs. Commissioner of Internal Revenue, *Respondent.*	Petition for review of a decision of the Tax Court of the United States.
No. 14467	

This cause came on to be heard on the transcript of the record from the Tax Court of the United States and was argued by counsel.

On consideration whereof, it is ordered and adjudged by this court that the decision of the Tax Court of the United States entered in this cause on February 21, 1963 be, and the same is hereby, Affirmed, in all respects in accordance with the opinion of this Court filed this day.

APPENDIX C

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT
Chicago, Illinois, 60610

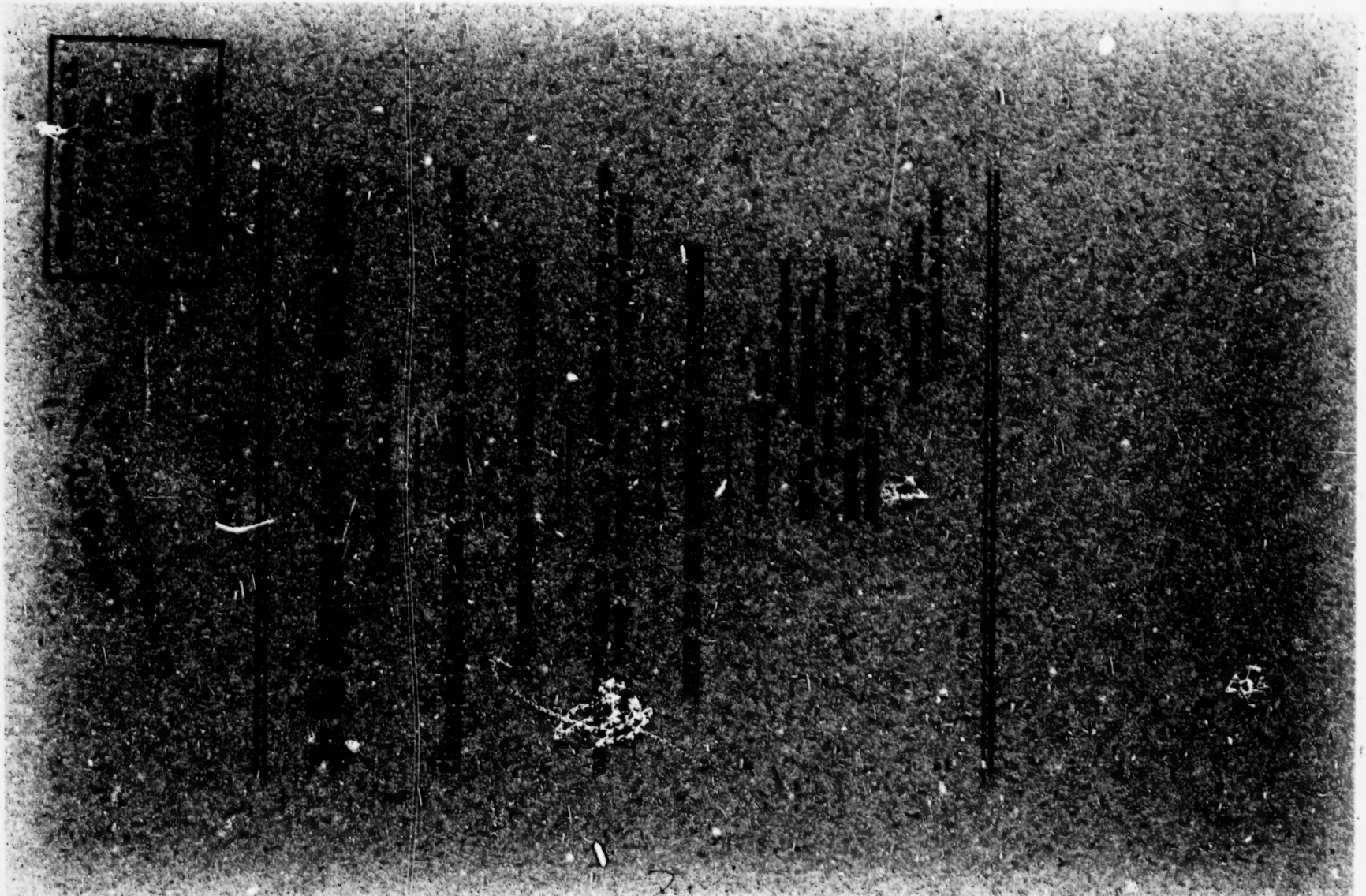
Tuesday, March 17, 1964

Before

Hon. JOHN S. HASTINGS, *Chief Judge*
Hon. ELMER J. SCHNACKENBERG, *Circuit Judge*
Hon. LUTHER M. SWYGERT, *Circuit Judge*

Charles Oran Mensik and Mary Mensik, *Petitioners,*	Petition for review of a decision of the Tax Court of the United States.
No. 14167	
vs.	
Commissioner of Internal Revenue, *Respondent.*	

It Is Ordered by the Court that the petition for rehearing filed by petitioners herein be, and the same is hereby Denied.



In the Supreme Court of the United States

OCTOBER TERM, 1964

No. 186

CHARLES ORAN MENSIK AND MARY MENSIK, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. 1a–8a) is reported at 328 F. 2d 147. The opinion of the Tax Court (R. 30–113)[1] is reported at 37 T.C. 703.

JURISDICTION

The judgment of the court of appeals was entered February 10, 1964 (Pet. 9a), and a petition for rehearing was denied on March 17, 1964 (Pet. 10a). The petition for a writ of certiorari was filed on June 15, 1964. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

[1] "R." refers to the appendix to petitioners' brief in the court of appeals. "Tr." refers to the original transcript of the record in the Tax Court, which has been filed with the Clerk of this Court.

738-506 64

QUESTIONS PRESENTED

1. Whether the Tax Court correctly concluded that petitioner[*] had received taxable income in 1956 as a result of overpayments for services made between corporations controlled by petitioner and subsequent "loans" to petitioner's associate.

2. Whether the Tax Court correctly concluded that at least part of the tax deficiency was due to fraud with intent to evade tax so as to warrant imposition of a fraud penalty.

3. Whether the fraud penalty was properly assessed against both petitioner and his wife, who filed joint returns.

4. Whether the Tax Court properly denied petitioner's request for rehearing.

STATUTE AND OTHER AUTHORITIES INVOLVED

Internal Revenue Code of 1954:

> SEC. 61. GROSS INCOME DEFINED.
>
> (a) *General Definition.*—Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:
>
> (1) Compensation for services, including fees, commissions, and similar items;
>
> (2) Gross income derived from business;
>
> (3) Gains derived from dealings in property;
>
> * * * * *
>
> (26 U.S.C. 1958 ed., Sec. 61.)

[*] For the sake of convenience, C. Oran Mensik is referred to as "petitioner," although his wife, Mary Mensik, is also a petitioner by reason of having filed a joint return with her husband for the 1956 tax year.

SEC. 6653. FAILURE TO PAY TAX.

(a) *Negligence or Intentional Disregard of Rules and Regulations With Respect to Income or Gift Taxes.*—

* * * * * *

(b) *Fraud.*—If any part of any underpayment (as defined in subsection (c)) of tax required to be shown on a return is due to fraud, there shall be added to the tax an amount equal to 50 percent of the underpayment. In the case of income taxes and gift taxes, this amount shall be in lieu of any amount determined under subsection (a).

* * * * * *

(26 U.S.C. 1958 ed., Sec. 6653.)

STATEMENT

The facts are set forth in detail in the findings of fact of the Tax Court (R. 30-66). The pertinent portions thereof may be summarized as follows:

During 1956, petitioner controlled several corporations, including City Savings Association, a mutual savings and loan association, of which he was managing officer, president, and chairman of the board of directors. He also had control over Melvin Building Corporation [hereinafter "Melvin"]. Although no Melvin stock was issued in his name, petitioner's relatives and other associates, who nominally held the stock, took instructions from petitioner regarding the conduct of Melvin's business (R. 35-39, 82).

Melvin was in the real-estate and construction business, and all of its construction work in 1956 was financed either by City Savings or by some other financial institution controlled by petitioner. From

September 1955 to March 1956, Melvin remodeled the City Savings Building. Petitioner instructed Melvin's accountant to add additional fictitious costs to the remodeling job and to alter the records so as to reflect the total cost to Melvin as $256,207.26, instead of an actual cost of $115,397.71. City Savings then paid Melvin $367,800 (R. 36, 39–40, 43–44).

Orville Hodge, Auditor of Public Accounts of the State of Illinois, issued charters to some of the financial institutions controlled by petitioner and retroactively approved the investment of 10 to 15 percent of these institutions' assets in their own buildings, under a provision of Illinois law which requires any such investment in excess of 5 percent to be approved by the auditor. On May 11, 1956, City Savings loaned $200,000 to Hodge, secured by a mortgage on certain property in Fort Lauderdale, Florida. At petitioner's request, Melvin transmitted $76,312.50 to Hodge on March 12, 1956, for which Hodge executed an unsecured 90-day judgment note. Petitioner represented to Melvin that the "loan" would be repaid from the proceeds of the City Savings mortgage. On June 29, 1956, Melvin issued two more checks for $50,000 each, for the purpose of lending $100,000 more to Hodge. One check was made payable to cash, and the currency was delivered to petitioner. The other check was made payable to City Savings and was endorsed by it. Two more unsecured judgment notes in the amount of $50,000 each, bearing no due date, were executed by Hodge on June 29, 1956. Hodge, who was shortly thereafter charged with embezzling State funds and was subsequently convicted, never

repaid either the $76,312.50 or the $100,000 "loan" (R. 44, 46–48).

On July 17, 1956, two days after Hodge was charged with embezzlement, petitioner borrowed $200,000 from Melvin to buy the mortgage on the Fort Lauderdale property from City Savings. Petitioner then gave Melvin a five-year judgment note for $200,000, payable at four percent.

On the basis of these transactions and others which are not relevant here, the Commissioner of Internal Revenue entered a deficiency jeopardy assessment for 1956 in the amount of $547,967.55, plus a fraud penalty of $273,983.78 (R. 64). The Tax Court found a deficiency of $201,022.33,[1] and held that part of the deficiency was due to fraud with intent to evade. Hence it concluded that a 50 percent addition to tax was warranted (R. 1). Petitioner filed a motion for rehearing (Tr. 975–988; R. 113–122, 127–131) which the Tax Court denied (Tr. 1039).

The Court of Appeals affirmed the Tax Court (Pet. 7a.) Both courts found that overpayment of City Savings funds to Melvin, under the guise of pay-

[1] In this Court, petitioner apparently challenges only the validity of the Tax Court's finding with respect to the $176,312.50 "loaned" to Hodge. The other seven findings (R. 31–33) are not challenged.

[2] The Tax Court permitted the Commissioner to amend his answer (Tr. 115; R. 26–27), in which he asserted (Tr. 116; R. 27–28) that one item of unreported income, originally determined to be $176,312.50 (R. 65), relating to petitioner's omission of income from City Savings, should have been $376,312.50. The Tax Court, however, sustained the original determination as to this item, and the Commissioner did not appeal from that decision.

ments for the remodeling of the City Savings Association Building, was advisedly arranged by petitioner, and that part, if not all, of the overpayment was thereafter paid by Melvin to petitioner and to Hodge on petitioner's behalf. (R. 55, 66-95.)

ARGUMENT

This case involves only the resolution of factual issues regarding petitioner's transactions in 1956. Both courts below resolved these issues against petitioner. There is no conflict in decisions, and no question of general importance is presented by this case.

1. The deficiency of $76,312.50, which petitioner challenges, represents overpayments made by City Savings to Melvin on the remodeling contract, which ultimately were paid to Hodge, in the guise of loans, on petitioner's instructions. The evidence demonstrated that the original estimate for the job was $125,000, that the actual total cost was $115,297.71, and that Melvin was paid $337,800. (Tr. 563-569, 699-700, 737-738; R. 10-11; Ex. V.) Petitioner directed that false entries be made in Melvin's books to conceal the true profit and to overstate the actual costs. (Tr. 384-387, 491-493, 570-574, 609-611, 622-626, 724-736; Exs. S, V.)

The receipts, funds were funneled from Melvin on petitioner's instructions. As the Tax Court observed, it was not coincidental that the $76,312.50 "loan" to Hodge was consummated shortly after payments were made from City Savings to Melvin in the amounts of $45,000 and $61,000. And the two $50,000 checks representing a "loan" to Hodge on June 29, 1956, in amounts actually received in cash by petitioner—closely

followed payments of $46,800 and $43,000 on the remodeling job.

The Tax Court was, therefore, fully warranted in concluding that the payments to Hodge were actually "made for the account of petitioner" and that he, not Melvin, was to "be the ultimate recipient" (R. 111-112). Petitioner's contentions (Pet. 11-15) that he realized only Hodge's "favors" as a result of these transactions and that he personally received no part of these "loans" misapprehend the basis of the Tax Court's findings. It is because petitioner fully controlled the disposition of the overpayments made to Melvin that such amount was taxable to him. See, *e.g.*, *Helvering* v. *Horst*, 311 U.S. 112. The fact that the money was paid to Hodge—possibly, as the Tax Court observed, in exchange for "favors" done on petitioner's behalf—did not prevent it from being income to petitioner; nor did it make the value of the "favors," rather than the "loans," the actual measure of petitioner's gain from these transactions.

2. The evidence was more than adequate to establish fraud. Petitioner's conduct with respect to Melvin's books and records demonstrated that he was deliberately concealing the nature of Melvin's profit. In addition, the payments to Hodge were falsely reflected on Melvin's books as "loans," although there appears to have been little intention to make repayment to Melvin (Tr. 447-450, 468-469, 646-655, 705-711; Exs. K, L, W, A, D, A, E, A-J).

3. There is no merit to petitioner's contention that his wife, who was not shown to have been personally involved in any fraud, may not be [illegible]

fraud penalty (Pet. 19–20). Since she signed the joint return she is subject to the joint and several liability imposed by the statute. *Ginsberg's Estate* v. *Commissioner*, 271 F. 2d 511 (C.A. 5); *Farnish* v. *Commissioner*, 262 F. 2d 727 (C.A. 9); *Prokop* v. *Commissioner*, 254 F. 2d 544 (C.A. 7); *Kann* v. *Commissioner*, 210 F. 2d 247 (C.A. 3), certiorari denied, 347 U.S. 967; *Boyett* v. *Commissioner*, 204 F. 2d 205 (C.A. 5); *Howell* v. *Commissioner*, 175 F. 2d 240 (C.A 6). *Cirillo* v. *Commissioner*, 314 F. 2d 478 (C.A. 3), cited by petitioner (Pet. 20), is inapposite. There the wife was not subject to the imposition of the fraud penalty because she did not sign a timely joint return. The fraud consisted of the failure to file a timely return.

4. In denying petitioner's motion for rehearing (Tr. 1039)—an action which the court of appeals sustained (Pet. 7a–8a)—the Tax Court acted well within its authority. The grant or denial of a motion for rehearing is within the sound discretion of the Tax Court. *ABC Realty Co.* v. *Commissioner*, 295 F. 2d 98 (C.A. 8); *Traum* v. *Commissioner*, 237 F. 2d 277 (C.A. 7); *Leaton* v. *Commissioner*, 237 F. 2d 5 (C.A. 7). Having found that petitioner was to "be the ultimate recipient" of the money paid to Hodge irrespective of whether these payments "were intended as a payoff or as loans" (R. 111–112), the Tax Court could legitimately conclude that Hodge's testimony could not affect the result it reached.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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IN THE

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OCTOBER TERM, 1963.

CHARLES ORAN MENSIK and
MARY MENSIK,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

REPLY BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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August, 1964.

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REPLY TO RESPONDENT'S BRIEF IN OPPOSITION TO THE PETITION.

The Respondent's brief in opposition to the petition for the Writ of Certiorari contains a new theory by which Respondent seeks to justify the finding of the Tax Court that the Petitioners had taxable income as a result of the loan by Melvin Building Corporation to one Orville E. Hodge. Both the Tax Court and the Court of Appeals made "favors received or to be received" by the male Petitioner from Orville F. Hodge of no determinable monetary value or no value at all, the conjectural measure of tax liability and fraud penalties. Now Respondent argues:

> "Petitioners' contentions (Pet. 11-15) that he realized only Hodge's "favors" as a result of these transactions and that he personally received no part of those 'loans' misapprehend the basis of the Tax Court's findings. *It is because Petitioner fully controlled the disposition of the [illegible] payments made to Melvin that such amount*

was taxable to him." (Resp. br. p. 7) (Emphasis supplied.)

With this as a keystone, Respondents' brief then weaves threads of suspicion and theory and presents them as the cloth of fact. For these reasons, Petitioner deems a reply necessary. Parenthetically it should be noted that the entire history of the cause is one of shifting theories by the Internal Revenue Service and government attorneys, when answered by petitioners to alternative bases with consequent deprivation of *due process* to the Petitioners.

The starting point of this assessment against Petitioner is set forth in the original 90 day letter statutory notice of deficiency as follows:

> "Payments to you, or for your benefit by City Savings Association and Melvin Building Corporation in the total of $327,824.04."

Listed in this total as item C was the specific item in the amount of $176,312.50.

In preparation for trial, the attorneys for petitioners separately discussed this specific item of $176,312.50 with government counsel for Respondent. In reliance upon statements of government counsel . . . "You won't have to bring him in. We're not contesting that payment was made by Melvin to Hodge. . ." (See affidavits R. pp. 129 and 130) the attorneys for petitioners thereupon abandoned their thought of requesting subpoena for Hodge. On the day of trial Respondent shifted his position and filed amendment to pleadings changing this specific item from $176,312.50 to $206,330.16. In answer to petitioners' objection to this new theory, government counsel argued (Tr. 25):

> "*Exactly how he got his money out of Melvin, we cannot show* precise amounts, of course, and dates. We

> have a number of instances which we *think* could very well constitute his taking money out of Melvin. One of them was a loan by Melvin to Orville E. Hodge, who is now in prison, the State Auditor who was a friend and benefactor of Mensik's; *and that was used in the 99 day letter as the measure of the misappropriation from this job.*" (Tr. 33) (Emphasis supplied)

The Tax Court overruled petitioners' objection and allowed the amendment, in derogation of petitioners' right to have sufficient time and opportunity to meet Respondent's new theory of the case. It is to be noted that the case was submitted on the amended theory just five days later on June 29, 1959 when Judge Bolon B. Turner took final submission of the case. A year and one half later the Tax Court rendered its decision and in rejecting the amendment fell back on the presumption of correctness of the original statutory notice of deficiency, this, despite conceded error and inaccuracies of more than 60 per cent of the amounts assessed—being more than $500,000.00 of the asserted tax and penalty.

> The errors and inaccuracies of this notice of deficiency included: an arbitrary disallowance of petitioners' payments of interest on personal loans in the amount of $11,308.10.
>
> The petitioners' payments of real estate and sales taxes in the amount of $1,440.92, including local real estate taxes on the home in which petitioners live.
>
> Charitable contributions made by petitioners totalling $2,380.00.
>
> An assessment of $1,30,416.36 as income on monies borrowed by Petitioners from the Chicago National Bank and the Oak Park National Bank upon which petitioners were paying interest.
>
> A disallowance of all original purchase cost of $49,567.66 for real estate which was sold during the pertinent year.

Disbursements from an escrow account in the amount of $60,000.00 charged as income to petitioners.

Denial of business travel expense by male petitioner in the amount of $4,614.63.

An Allied Investment Company check in the amount of $70,096.91 charged as income to petitioners."

It was not until one year after the proceedings were commenced that the Commissioner Respondent conceded error to all the above items and so stipulated in the Tax Court.

The decision none the less was bottomed on "favors received or to be received." (R. 94). After the Tax Court's decision a petition for rehearing was filed and petitioners sought to bring in the witness Hodge having thus learned that the question of "favors" governed the Tax Court's decision. This was crucial because the language of the Tax Court (R. 94), "*We do not know what the full and true story is with respect to the payments by Melvin to Petitioner in 1956*" . . . and "*what the arrangement was between Petitioner and Hodge, we do not know*" . . . is an outstanding admission that the Court itself had not resolved the very issues upon which it rested its decision that petitioners were in receipt of unreported income in the amount of $176,312.50. In the view taken by the Tax Court Judge of this aspect of the case, Hodge's testimony was vital. To refuse the petitioner's right to call this witness was not a mere exercise of discretion but serious and substantial error and petitioners were thus denied *Due Process of Law*.

The history of this cause reflects a continuous slanting of evidence to meet new theories when answered by petitioners to justify assertion of tax by the Commissioner of Internal Revenue against petitioners for the $176,312.50 transactions between the Melvin Corp. and Hodge. For a time "favors" was the basis. Now at this stage of the litigation Respondent adopts a new theory.

The Respondent's present position: "It is because petitioner fully controlled the disposition of the overpayments made to Melvin that such amount was taxable to him." is found in the Respondent's brief at page 7. This statement is followed in the next sentence by the confusing assertion: "the fact that the money was paid to Hodge, possibly, as the Tax Court observed, in exchange for "favors" done on Petitioner's behalf—did not prevent it from being income to petitioner; nor did it make the value of the "favors", rather than the "loans, the actual measure of petitioner's gain from these transactions." The reason for this constant shifting is obvious. The Respondent and the Courts below do not say why money from Melvin to Hodge is income to the petitioners, other than by arbitrary declaration. The Melvin Building Corporation reported this income from the City Savings Association remodeling job and paid tax on the income. Melvin Building Corporation made loans to Hodge of $176,312.50 yet the Commissioner has assessed this same item as income to Hodge. This same item, to the penny, is here being assessed against these petitioners as income to them, therefore the petitioners must continue to assert that they will be deprived of property *without Due Process of Law* by the flow and ebb of the governmental processes.

The fact recitation by the Respondent contains some major inaccuracies:

Inaccuracy No. 1: (Resp. br. p. 3)

> "* * * petitioners' relatives and other associates, * * *, took instruction from petitioner regarding the conduct of Melvin's business."

Correction:

The record does not bear this out. Respondent has cited several record references (R. 35-39, 82). The pertinent portions, thus referred to, upon closer examination do not justify such a conclusion. The Tax Court actually said:

> "In transactions in which petitioner had an interest directly or indirectly and with which Carl Melberg, Kramer or Mary Ann Barto were involved or concerned, they were subservient to petitioner, and where Melvin was a party to such transactions, petitioner, to a substantial degree, determined and directed the manner of their treatment on Melvin's books."

If it was conceived for argument purposes that petitioner C. Oran Mensik *did* "to a substantial degree, determine(d) or direct(ed)" the manner of their treatment on Melvin's book," then it must be remembered in this connection that Melvin did report this *total* income and its source and paid income taxes. This is unquestioned, it is a construction of disbursement of loans that is questioned.

Respondent would have this Court believe that petitioner was actually running Melvin's business. The number of times when he was consulted in no way justify the Respondent's conclusion of constancy. On such occasions Melberg, the President of Melvin; was *always* present and the clear and correct interpretation to be given these conferences is that petitioner's advice on financial matters was frequently sought on extra work done.

There is no evidence that petitioner imposed himself upon the conduct of Melvin's business. The brief of the Respondent also refers to p. 82 of the record. Reference to that record shows that the Tax Court said:

"As between petitioner and Melvin, the record shows that Monsik was likewise in a position of dominance, and where his personal interests were concerned, that he did dominate."

This is a far cry from the Respondent's assertion that the male petitioner directed and instructed regarding the conduct of Melvin's business.

Inaccuracy No. 2: (Resp. br. p. 4)

"Petitioner instructed Melvin's accountant to add additional fictitious costs to the remodeling job and to alter the records so as to reflect the total cost to Melvin as $256,207.26, instead of an actual cost of $115,397.71."

Correction:

No actual cost was established. The record fully discloses the Tax Court's confusion on this point. There is a concession that added costs increased the original estimate. (R. 70-72).

It is significant that the Respondent's brief makes no record citations to the direct examination of government witness Joseph W. Bagnuola, the independent architect who prepared the original plans for the City Savings Association remodeling. This testimony (Tr. 427-446) clearly explains the reasons for the disparity between the original estimate of the job ($125,000.00) and the final payments by City Savings Association to Melvin of $367,800.00. Many additional changes had to be made as work progressed and

additional charges not contemplated at the time the original plans were made.[1]

It is also significant that this government witness also testified, in detail, to the many items not included in the original estimate of $125,000.00 (the amount referred to by respondent at page 6 of the brief in opposition to review). These items were substantial:

> In connection with the original estimate of $125,000.00, the architect when examined by the government attorney for the Internal Revenue Service stated that air-conditioning on the second floor to all rooms, was not included (Tr. 434).
> Cement sponge base and rubber tiling for flooring on the second floor. Not included (Tr. 435).
> Heating for second floor. Not included (Tr. 435).
> Reinforcement of roofing (which architect estimated as an additional $10,000.00 cost for this one item. Not included (Tr. 436).

[1] (Tr. p. 431) A. Yes. I was called in on many occasions due to the structural findings of the building. In any re modeling job, there are always hidden factors that we cannot anticipate until we open up the construction features. And in one instance, I was called in to redesign the roof structure of the west portion of the second floor addition because the partition walls which were constructed were supporting walls; and when we removed them, the joists were sagging. And additional steel had to be inserted in order to re-enforce the roof structure. There were about six or seven beams involved. We had to design the beams. These beams had to be inserted in the walls and the roof had to be shored up so the beams would fall in line with them there.

We were also called in on another instance on the elevator shaft. The existing masonry wall which is a bearing wall that is supporting a four story building—I believe it is three or four stories—and the foundation is constructed of rubble stone which indicated the building was at least fifty years old or more. We had to undermine underneath the existing wall and privide shoring and additional footings in order to install this elevator.

Painting on second floor. Not included (Tr. 439).
Installation on cel-o-tex ceilings on second floor. Not included (Tr. 439).
While the bank was operating during normal business days payment of overtime for evening work and Sunday work. Not included (Tr. 439).
Terraza floor on the main floor of the bank. Not included (Tr. 441).

These and many other changes in the remodeling job made it necessary for the male petitioner in his capacity as an officer of the City Savings Association to meet with Mr. Carl M. Melberg, President of the Melvin Building Corporation on many occasions. It was also necessary for Mr. Mensik to meet with the accountants of the Melvin Building Corporation, particularly Mr. Leon Winterhalter of Burlingame and Company, Certified Public Accountants with offices in Chicago and St. Louis. Further in connection with the alleged entries in the Melvin books it is to be noted that the record is clear that whenever Mr. Mensik conferred with the bookkeeper, Mr. Melberg was also present. The inference drawn by the Tax Court that Mr. Mensik directed entries to overstate the true profit is unfounded in this record.

Reason dictates that the male petitioner did not control or dominate the book entries made by the Melvin Building Corporation and the practices of this accounting firm. In view of the clear requirement that to assess fraud penalties there must be a clear and convincing showing of "fraud" that burden simply was not met nor established in this case. The piling of inference upon inference or inferring that circumstances are suspicious has given rise to comment by many courts. We submit the following language of the United States Court of Appeals, Second Circuit, to be particularly appropriate here:

> "When it comes, however, to his proof on the issue of fraud, where the burden lay on the commissioner, we think that it fails as proof for lack of evidence of a starting or an ending point. While it is true that the taxpayers proof and attitudes, not only in this matter but in matters where she came in conflict with the Office of Price Administration, was not satisfactory, this did not supply the deficiencies in the commissioners proof, which, despite his contention here to the contrary, consisted of little more than the fact that he had determined the deficiency claimed. The case on the issues where the burden was on the commissioner was presented and tried too much on the theory, 'Give a dog an ill name and hang him'." *Olinger* v. *C.I.R.*, 5 Cir., 234 F. 2d 823, P. 824.

The constant repetitive use of "the petitioner" by the government and the lower courts shows the *pro forma*, casual, and arbitrary failure of consideration to the position of Mary Mensik, *Petitioner*. The title of the case emphasizes this error.

Mary Mensik only signed the return as a spouse with reliance on accountants and her husband. Not a scintilla of evidence indicates her participation or knowledge of these transactions of her spouse, in any matter covered by the record. How can it be conceived under this record of evidence that the Commissioner respondent, has proved clearly, or at all, that she had the mental attitude of fraud. If she was negligent, at worst, it is arbitrary deprivation of *due process* to brand this lady with fraud on this record.

Inaccuracy No. 3 (Resp. br. p. 4):

> "Orville Hodge, Auditor of Public Accounts of the State of Illinois charters to some of the financial institutions controlled by the petitioner and retro-

actively approved the investment of 10 to 15 per cent of these institutions assets in their own buildings, under a provision of the Illinois law which requires as such investment in excess of 5 per cent to be approved by the auditor."

Correction:

Note: This correction brings the petitioners to another assignment of error below. It has been contended that when the Tax Court refused to grant the petition for rehearing, the petitioners were denied due process. The truth was also suppressed. The government says in its brief here that Hodge's testimony "could not effect the result it reached" (Resp. br. p. 8). This ignores the real basis for imposing upon petitioners a tax on $176,312.50 received by Hodge from Melvin. The inaccuracy stated above is prelude to establishing a *quid pro quo* for the loans by Melvin to Hodge and taxed to the petitioners. Testimony by Hodge fortunately is a matter of record here. It takes two forms. The first is a Q and A taken by Intelligence Agents of the Internal Revenue Service from Hodge on November 13th, 1958, after he was incarcerated in the Illinois State Penitentiary at Menard, Illinois (R. 115-122). The other is an affidavit by Hodge given while still in the penitentiary on March 30th, 1962. (R. 127-9)

Hodge, in addition to swearing on both occasions that he received the $176,312.50 and used it in the construction of his Esquire Hotel in Florida, states several items of crucial importance to the issues before the Tax Court:

Q. New buildings were erected on the sites acquired. One on North Ashland Avenue and the other on North Avenue in Chicago. These buildings were completed about July of 1956. It appears that the costs were much in excess of allowable expendi-

tures for construction based on deposits. Did you approve the excessive costs on these buildings.

A. I had nothing to do with that department whatsoever and I didnt even know they had two buildings. (R. 121)

It should be clear that "excessive costs" as here used does not refer to cost of construction of the buildings which were later sold for book value.

And, again on the subject of "favors":

Q. Could these so-called loans have represented a consideration of any favor that you may have granted Mr. Mensik or his association?

A. I never gave Mr. Mensik any more favors than I gave any other loan associations in Chicago or the State of Illinois. (R. 122)

In his affidavit Hodge stated:

"Your affiant states that, if he were unable to pay back the $176,312.50 to Melvin Building Corporation within the year, affiant intended to issue a second mortgage to Melvin Building Corporation on the Esquire Hotel in Miami, Florida. Affiant states that the said hotel, in affiant's opinion, was worth at least $700,000.00, and that, at a forced sale, and under peculiar circumstances, it was sold for $575,000.00. Affiant felt that a total mortgage of the amount of $376,312.50 was an amount well within the actual value of the said property.

Your affiant regarded the loan from Melvin Building Corp. as a pure business deal, and your affiant, in his private and official capacities, did no favors for C. Oran Mensik in return for the loan of this money, or any other monies." (R. 128)

The mortgage referred to by Hodge, of course, INCLUDED THE $176,312.50 LOANED HODGE BY MELVIN.

The Tax Court ignored this plain testimony which clearly corroborated the petitioners' evidence. No evidence to the contrary was adduced by the Respondent. The "theory" of the Internal Revenue Service has been accepted by the Tax Court in lieu of sworn testimony. To reject it or ignore it under the circumstances was error and a deprivation of *due process of law.*

Aside from the fact that the Tax Court has attacked the rate of profit earned by Melvin, for the remodeling, the Tax Court further found that the contract was so awarded "with the deliberate purpose of providing funds for the payment" by Melvin to a former public official, one Orville Hodge. The first loan to Hodge was made by the Melvin Building Corporation on 3/12/56 for $76,312.50, more than six months after the original remodeling contract was executed and the balance of the sum in question, $100,000.00, was loaned on June 29, 1956, nine months after the building contract was executed by the officers of City Savings and the directors of said mutual Ass'n. How ca nany presumption be drawn that the contract was entered into as a means of providing funds to Melvin so as to make payments to a state official, when there is a lapse of 9 months between both events? The inference of the Tax Court that since payments were mad. by City Savings Assn. to Melvin Building Corp. in amounts similar to the amounts of the loans to Hodge was not just *coincidence*, can hardly be a sound basis upon which to sustain imposition of fraud penalties in excess of $100,000.00.

At Page 6 of the governments brief it is argued, "Thereafter, funds were funnelled from Melvin on petitioners instructions." Funnelled to whom? The record clearly shows it was Hodge who received the money and exe-

cuted three judgment notes to secure repayment and yet the commissioner now stands on the proposition (Page 8 Respondent's brief), that the "Tax Court found that petitioner was to "be the *ultimate* recipient." The record is void of showing that Petitioners received a single penny of this money.

The Respondent cites *Helvering* v. *Horst*, 311 U.S. 112, in support of its position. This case is inopposite to the facts here and concerns the gift of negotiable interest coupons not then due, from father to son. This was property held by the Father *as a matter of right* and the sole question as stated by this court at page 114 was:

> "The sole question for decision is whether the gift, during the donor's taxable year, of interest coupons detached from the bonds, delivered to the donee and later in the year paid at maturity, is the realization of income taxable to the donor."

It is respectfully submitted that the record in the instant case shows that the court below departed from established principles of decision in finding that petitioners *realized gain* upon which income tax can be properly asserted and that the Respondent failed in its burden to establish fraud. For the reasons stated hereinabove the petitioners respectfully seek relief from this court.

CONCLUSION.

Respondent's brief opposing review fails to meet petitioners' contentions. Petitioners seek certiorari to review all issues decided by the lower court. It is respectfully submitted that substantial issues are involved which include *due process of law* as guaranteed by the Constitution of the United States to all of its citizens and that the lower court in adopting the opinion and findings of the Tax Court "in all respects", so far departs from the usual course of judicial proceedings and established principles of decision as to call for an exercise of this Court's power of supervision.

Respectfully yours,

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